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<u>Japan's Economic Policy</u> 25X1

Domestic pressure to trim government budget deficits and foreign criticism of the yen's weakness are limiting Tokyo's efforts to pull the Japanese economy out of a protracted slump. Committed to reducing the government deficit, Prime Minister Nakasone has endorsed a harsh FY 1983 (April 1983-March 1984) budget that authorizes only a 1.4-percent rise in spending. Transfers to local governments will be slashed to permit moderate increases in defense and foreign aid outlays. With inflation tamed, Japanese authorities could loosen monetary policy if they desired. The Governor of the Bank of Japan is sensitive to foreign charges that the yen is undervalued, however, and refuses to cut the official discount rate until the currency has strengthened. We do not expect the Nakasone government to reverse these conservative economic policies and adopt anti-cyclical measures unless the ruling Liberal Democratic Party fares poorly in upcoming elections. Barring such a policy shift or a remarkably rapid recovery in the OECD, the country is headed for another year of slow--by Japanese standards--economic growth. 25X1

This memorandum, requested by James Murphy, Assistant Special Trade Representative, was prepared by Japan Branch, Northeast Asia Division, Office of East Asian Analysis. Information available as of 3 February 1983 was used in its preparation. Comments and queries are welcome and may be directed to the Chief, Japan Branch, Northeast Asia Division, OEA, 25X1 25X1

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We foresee Japan's trade and current account surpluses rising to $23-25 billion and $10-12 billion respectively in 1983. The combination of price competitiveness enhanced by a weak yen and slow economic recovery overseas should stimulate exports, while weak oil and raw material prices hold down the import bill. Last year, Japan's worldwide trade surplus totalled $18.2 billion. Exports--motor vehicles and consumer electronics in particular--declined in both volume and value as global recession and export restraints more than offset the effects of the yen's weakness. Imports also fell in value because of soft oil and raw material prices. At the same time, income from rapidly growing overseas investments pushed Japan's current account surplus up from $4.8 billion in 1981 to $6.9 billion. [redacted] 25X1

Specific Trade Issues

Automobile Export Restraints

Officials in both the Japanese government and auto industry recognize that continuation of the 1.68-million-unit-per-annum quota through March 1984 is virtually unavoidable, but they have been unable to agree on extending restraints into JFY 1984. Although MITI negotiatiors initially will point to the recent upturn in US auto sales and argue for increasing the 1.68 million quota as a counter to an expected US demand for a cut to 1.3 million, they are prepared to settle for a third year extension at current levels, [redacted] MITI also 25X1 recognizes that Japan may have to accept the concept of a fourth year of restraint to help stave off protectionist measures being proposed in the US Congress, but will probably ask for postponement of detailed negotiations until next year. Neither MITI nor the auto companies have given any indication that they have seriously considered cutbacks in the JFY 1983 quota. If Washington insists on cutbacks, MITI would be forced to undertake a time-consuming effort to reconcile the conflicting interest of the companies. A reduction in the quota would also weaken Tokyo's ability to withstand Canadian and Western European demands for export restraint. [redacted] 25X1

Standards and Certification

The proposal to draft a comprehensive "Market Liberalization Promotion Law" that would simplify existing import inspection and certification procedures will provide a test of Prime Minister Nakasone's ability to move reluctant bureaucracies in a direction dictated by broad national interests. We expect the "Liaison and Coordinating Headquarters" established to draft the new law to be

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delayed by pleas for special exceptions and plans for special promotion measures. [redacted] MITI officials will: 25X1

-- Abandon specific nontariff barriers such as the "S" mark for aluminum baseball bats in order to alleviate pressures for general liberalization.

-- Establish organizations such as the proposed Machinery Import Research Institute to join with the Japan Machinery Importers Association in an effort to double machinery imports. This proposal would create a new unofficial bureaucracy to help foreign companies work their products through the standards and certification system rather than reduce or simplify existing procedures. In the end, however, importers will have to pay the costs of the additional bureacracy and therefore raise the prices of imported machinery. [redacted] 25X1

To help keep the focus on across-the-board reforms, the US may find it useful to maintain channels of communication not only with MITI and other affected ministries, but also with groups such as the LDP's Special Research Committee on International Trade (the Esaki Committee), the Chief Cabinet Secretary's office, the Economic Planning Agency, and the Ministry of Foreign Affairs, which have no vested interest in the existing system. [redacted] 25X1

Restraining Exports to the EC

For the past three weeks the Japanese press has been reporting EC requests that Japan voluntarily restrain exports of as many as 10 commodities--automobiles, color televisions, color television tubes, NC machine tools, video tape recorders, light commercial vehicles, motorcycles, forklifts, audio equipment and quartz watches. Tokyo reportedly is interested only in discussing restraints for VTRs, the only one of the 10 to show a substantial increase in exports to the EC during 1982. In the past the Japanese preferred to negotiate restraints with individual member countries rather than through the EC Commission. By discussing VTRs with the Commission, Tokyo probably hopes to enlist broader EC support for its protests against French nontariff barriers to VTR imports. [redacted] 25X1

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